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Requirements of a Philosophy of Money and Finance

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Abstract:

Geoffrey Ingham is a distinguished economic sociologist and political economist who has contributed greatly to the development of a sorely-needed genuine “monetary science” as opposed to the limited scope of “monetary economics” as usually defined. A notable feature of his work has been his “long-standing impatience with the disciplinary boundaries of the social sciences in academia” and a concerted effort to break them down. This paper accepts Ingham’s position that a full understanding of monetary and financial issues will require a far more interdisciplinary approach than is currently the norm in academia. Specifically, it is argued there would need to be a combination of a realist social ontology, economic sociology, monetary macroeconomics, and political economy.

These requirements seem correspond to the different branches of philosophy itself, ontology, epistemology, ethics and politics. In the double scheme, the second and third categories from the first list correspond to the second category from the other one. Economic sociology and monetary macroeconomics together *comprise* the relevant epistemology. Similarly, the subject of political economy corresponds to ethics and politics. This is the point at which the ethical and political dimensions become relevant.

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Introduction

Geoffrey Ingham is a distinguished economic sociologist and political economist who has contributed greatly to the development of a (sorely-needed) genuine “monetary science” (Mendoza 2012) as opposed to the limited scope of “monetary economics” as this is usually defined. A notable feature of his work has been his “long-standing impatience with the disciplinary boundaries of the social sciences in academia” (Ingham 2004) and a concerted effort to break them down. In previous work (Smithin 2009, 2011), I have similarly argued that a full understanding of monetary and financial issues (and therefore of “economic issues” in general)[2] will require far more of an interdisciplinary approach than is currently the norm in academia. This chapter, therefore, accepts Ingham’s position essentially without reservation.

In what follows, the first section of the chapter identifies each of the academic disciplines (*if* that is the right word) that seem to be relevant, and how they relate to the traditional branches of philosophy itself. This is the origin of the idea of the "requirements" for a philosophy of money and finance. Later sections then address, in turn, a number of the obvious questions arising from the overall scheme and make some attempt to answer them. Particular attention is paid to Geoff Ingham's home discipline of economic sociology, and to the philosophical gulf that exists between that field of study and the mainstream/neoclassical notion of microeconomics or micro-foundations.

Interdisciplinary Approaches to the Economy, Business, Money and Finance

According to Smithin (2009, 2011), a realist approach to monetary and financial issues able to effectively cross interdisciplinary boundaries would require study in *each* of the following fields (in order):

(1) A Realist Social Ontology

(2) Economic Sociology,

(3) Monetary Macroeconomics; and,

(4) Political Economy.

The term *realism* is used in the sense of (*e.g*.) Searle (1995, 2010) or Mendoza (2012), and the term *ontology* as in the work of Lawson (1997, 2003) or Kim (2011). The argument is that there needs to be developed a realist ontology of the underlying social institutions relevant/necessary to the conduct of economic activity. It must include all such things as business firms, money, banks, governments, *etc.* In short, there has to be an investigation of the basic *nature* of social institutions and social facts (Searle 2010). Geoffrey Ingham's most important book is entitled *The Nature of Money* (2004). It is particularly important to stress the large difference in kind between the "social facts", and the facts of the physical or biological world, the so-called "brute facts" studied in natural science. Searle (1995), for example, wrote extensively about this in his *Construction of Social Reality*. I think that it is vitally important to note that the title of Searle's book was *not* the ~~*Social Construction of Reality*~~.

Next, the idea of economic sociology implies a study of the *specific* social institutions in a given socio-economic system. The research problem of the pioneering economic sociologist Max Weber (2003/1927), for example, in the *General Economic History* was to decipher the "meaning and presuppositions of modern capitalism", also known as the "method of enterprise" (Collins 1986). Meanwhile, Schumpeter (1983/1934) wrote about *The Theory of Economic Development* set explicitly in the context of the institution of "capitalist credit-money" (Ingham 2004). Geoffrey Ingham himself recently published a book, entitled simply *Capitalism* (2008), dealing with the twenty-first century version of the phenomenon.

Monetary macroeconomics is (I would say) by far the most important "technical" field of economics. It has, of course, not coincidentally, been the main area of interest for a great many heterodox economists, including such groups as Post-Keynesians, circuit theorists, and contemporary adherents of MMT (modern money theory). The main thing to notice about this general area of research is the overwhelming emphasis on the qualifier *monetary*. Macroeconomics *is* monetary economics, nothing more, nothing less. The titles of Keynes's most important books, *A Tract on Monetary Reform* (1923), *A Treatise on Money* (1971/1930), and *The General Theory of Employment Interest and Money* (1964/1936) most certainly seem to have been intended to imply as much. The focus on money is, also, the essential reason *why* the social institutions of money itself, credit, banks, *etc., etc.*, need to be thought about in depth before the topic of macroeconomics can even get started. Geoff Ingham has written persuasively on this subject in an article "Some Recent Changes in the Relationship between Sociology and Economics", published in the *Cambridge Journal of Economics* in 1996.

Political economy, finally, deals with questions of policy and governance, comparative economic systems, notions of equity and income and wealth distribution. Ingham's (1984) book on *Capitalism Divided* was an important and well-regarded contribution to this field.

The requirements set out in the list (1) through (4) seem to correspond (with some overlap) to the different branches of philosophy as such. We could therefore set out a second list, again in order, as follows:

(I) Ontology,

(II) Epistemology,

(III) Ethics; and,

(IV) Politics.

.In the double scheme, categories (2) and (3) from the list of disciplines relate to category (II) from the philosophical list. The argument, therefore, is that economic sociology and monetary macroeconomics together *comprise* the relevant epistemology as opposed, particularly, to neoclassical microeconomics. Similarly, the subject of political economy in category (4) corresponds to ethics and politics in categories (III) and (IV). This is the point at which the ethical and political dimensions become relevant. A graphical representation of the correspondence between our two lists appears in *Figure 1* below:

Figure 1: Correspondences

(I)	Ontology	(1)	A Realist Social Ontology
(II)	Epistemology	(2)	Economic Sociology
(III)	Ethics	(3)	Monetary Macroeconomics
(IV)	Politics	(4)	Political Economy

In the next section of the chapter it will be necessary to highlight a few of the basic questions that might be asked about the overall scheme and its interconnections. Some of these will already have naturally suggested themselves in the mind of the reader.

Questions Arising

Figure 1 irresistibly recalls a quote from Simmel's *Philosophy of Money* (1978/1907), which runs as follows:

> Every area of research has two boundaries at which the process of reflection ceases to be exact and takes on a philosophical character … If the start of the philosophical domain marks, as it were, the lower boundary of the exact domain, then its upper boundary is where the ever fragmentary contents of positive knowledge seek to be augmented by definitive concepts into a world picture and be related to the totality of life.

However, it will soon be realized that the scheme of *Figure 1* really has *no* such boundaries. There is a "philosophical character" throughout. The implication is that although there certainly can be precision of a distinct kind in solving the various research problems, there cannot the sort of "exactness" that is (presumably or allegedly) found in the natural sciences. Once again, the subject matter is different.

This leads on to the question of the *type* of knowledge that is sought. There is a Greek word *episteme* (from the same root as epistemology) which is often translated as "scientific knowledge". Is this the sort of knowledge that we seek? Unfortunately, a problem already hinted at in the previous paragraph, the use of the modern term science in the financial or monetary context is likely to be misleading, for the primarily cultural reasons identified by Lawson (2003). It would be better to say something like an understanding of the "principles of things". Another type of knowledge might be labeled *technical knowledge.* In the present context, this would have to be thought of as the type of material learned in "functional courses" in business school, such as accounting, finance, marketing, *etc.*

In these courses the student learns about such things as the rules to be applied to double-entry book-keeping and balance sheets, and technical details about how the various financial instruments (e.g., stock and bonds) and their derivatives (*e.g*., options and futures), are supposed to work. I would say that a third type of knowledge, the notion of *practical knowledge* (also much praised, at least in lip-service, in business schools and similar arenas), is, in contrast, something quite different. The term suggests "hands-on" experience which *by definition* cannot be found in a college course. It is a clear case of "Do it Yourself". In the financial world, the sort of thing I have in mind in this case is something as simple as (*e.g.*) being physically able to turn on a computer and to actually buy and sell stocks or bonds.

I think it is clear that we must be mainly interested here in the *first* type of knowledge. As I have tried to impress on several generations of my students enrolled in business administration courses (perhaps without notable success for a great many individuals in that group, but not all), is that in the university setting we must surely be interested in the financial equivalent of *episteme*. There is not much use in "playing the market", for example, or knowing how some complicated financial derivative works, or even in earning an academic PhD in Finance, without some idea of the basic principles of credit and money. One question that I invariably ask at PhD oral examinations in fields like banking, finance, accounting *etc*., (and in economics) is: do "loans make deposits" or do "deposits make loans"? I leave it to the reader to guess the most frequent answer to this question, very often made after maybe seven or eight years of intense study of the topic, on the part of the person answering it.

It is crucially important to note where "ethics" and "politics" fit in as part of the overall logical scheme. Actually, it is not possible to discuss either of these until *after* the ontological and epistemological issues have been decided. There may well exist an "objective science of ethics", which was the *desiderata* of libertarian scholars such as Rothbard (1998), for example. The argument is *not* relativism or pragmatism. However, *nor* does it lead to the *a priori* system of ethics that Rothbard and others have argued for. Rather the implication is that the ethical scheme must be coherent in some sense. It must be consistent with the "way the world works". Smithin (2011) has argued that Weber was therefore correct in his insistence to a left-wing group of students that social science in the first instance should be *Wertfrei* (value free).[3] The reason for this is that, according to the sequence set out here, the ethical and political questions cannot reasonably be dealt with until after the ontological and epistemological issues have been decided. The ethical and political attitudes adopted must ultimately be compatible with the underlying nature (ontology) of the social reality (Smithin 2009).

What has Happened to Neoclassical "Microeconomics"?

What will certainly strike most economists, whether from the academic mainstream, or for that matter from many heterodox schools of thought, is the absence so far of any reference to the discipline of "microeconomics" in the discussion. Why does this not appear explicitly? The answer is that it does not really need to there. Once it is recognized that the term economic sociology *already* includes such things as value theory, pricing theory, the theory of the firm and the study of market behavior, the omission becomes entirely reasonable. This way of expressing it, however, puts the whole notion of "market forces" in its place (so to speak) in the broader social order rather than being the *only* thing discussed. Moreover, the ordering of the list (1), (2), (3), (4), makes it crystal clear that "the market" certainly cannot logically ever be the *first* thing discussed. Neither the concept of the market, nor the academic discipline of neoclassical microeconomics as it has developed over the years, is foundational in the sense definitely implied by the coinage of the term "micro-foundations".

We touch here on the issues raised in the recent work by John King (2012) on *The Micro-Foundations Delusion: Metaphor and Dogma in the History of Macroeconomics.* The very title of that work seems emphatic enough. It is worth inquiring further, however, into exactly what it is that King finds delusional. Specifically, these are the ubiquitous DSGE (dynamic stochastic general equilibrium) model of early 21st century mainstream macroeconomics, and its underpinning in the concept of the RARE individual (the representative agent with rational expectations). These constructs have simply ignored the requirement to develop a plausible social ontology. However, if King is dismissive of the modern literature on the "micro-foundations of macroeconomics", he is equally skeptical of the reverse notion of the "macro-foundations of microeconomics", which would presumably start at "point (4)" in the list (1), (2), (3), (4), and go from there.[3] In Smithin (2004) I had earlier expressed a more favourable view of this concept than does King, following Crotty (1980), and I do not withdraw those remarks. However, the suggested ordering of the list now seems to put the various issues into the correct relationship to one another, and therefore, in the end, seems to mirror King's position fairly closely as well as that of Ingham.

An "Iterative Sequence" as Applied to Economic Sociology

Another philosophical concept that needs further emphasis is the notion of "iteration" (Searle 1995, 1998, 2005, 2010; Smithin 2009). This is the idea that one set of social institutions builds on another in a logical sequence, as is already implicit in the idea of a"correct order". *Via* iteration, it is therefore possible to build up a cognitive structure of almost any degree of complexity from the apparently simplest of underpinnings.

Barrows and Smithin (2006, 2009) and Smithin (2011), for example, have argued that for the establishment of something like Weber's "method of enterprise", there must have been a sequential development of (again in order) the following series of social institutions/social facts:

(A) A "political settlement" of some kind.

(B) Money (including both of the concepts of the unit of account and a means of payment, and the existence of some method of credit creation).

(C) Private "property" (in the specifically legal sense, *not* the mere concept of possession)

(D) Markets

(E) Entrepreneurial business

Much of the debate in the mainstream economic literature focuses on the question of so-called "government interference" in the economy, and how government regulations, and so forth, may hinder economic development. Moreover, it is easy to see that some forms of government can be entirely predatory, such as the *ancien regime* in the eighteenth century, or Stalinism in the twentieth. Nonetheless, it should be also be clear that in the iterative scheme, as Ingham has always insisted, the existence of *some* form of state "authority" or "sovereignty" must be regarded as a pre-requisite for the establishment of commercial society in the first place. Consider, for example, the argument of the neo-chartalist school that "taxes drive money" (Mosler 2011, Wray 2012). This refers to the view that it is the ability of the state to levy taxes, as a matter of sovereignty rather than of confiscation, and not because of any "need" to finance government expenditures that is actually the foundation of the monetary system.

The term money involves *all* of the social phenomena that Ingham, among others, has insisted should be included under this rubric. These include, first; a money of account, second; a well-identified asset, not necessarily a physical asset, serving as the final/ultimate means of settlement, third, a developed financial/banking system that ensures secure credit relations. These are the necessary conditions for such things as price lists and rational accounting to come into existence. Ultimately, they are necessary for the very feasibility of a system of production that entails taking a long position in goods and services, and functions *via* the generation of profits calculated in monetary terms. As for the precise place of money in the sequence, Ingham (2004) quotes Weber as definitely asserting that “money is the father of private property”, not the other way around.

Property rights are important for such a society because in a system centred on the profit motive (and, for that matter, also on the receipt of wages for services rendered), it is important that the recipients of those income streams be able to control their final disbursement, and not be subject to arbitrary confiscation. As already stressed, this idea does not de-legitimize taxation in principle, particularly when thought of as an act of sovereignty rather than as confiscation. However, the concept of private property does imply a definite set of both economic and legal principles that sharply delineate the scope of taxation, if the system is to function.

As already mentioned, the idea that the market appears only in third place on the iterative list (A), (B), (C), (D), (E) would, no doubt, seem strange from the viewpoint of orthodox economic theory. From that perspective, market exchange is treated as co-extensive with economic activity. The market is supposed to be the mainspring of the whole system, based on a supposed “natural propensity to truck, barter and exchange”, as in the formulation of Adam Smith (1981/1976). On this view, markets *as such* perform all the necessary functions of providing information, coordinating activity, and ensuring productive efficiency. Moreover, money need not really be involved. In principle, all that is going on is precisely barter exchange. The supposed information content consists of just these barter exchange ratios, rather than (as in reality) basic accounting notions of profit. As against the primeval belief in the supremacy of the act of exchange, in actual social systems things are far more complicated. Both markets and market exchange, as they actually function in the real enterprise system, are built upon the *prior* institutions of money and private property.

“Exchange” for *money* finally slots into the picture primarily because, if there is to be a system in which the incentive for production is profit, actually quantifiable in monetary terms, and *not* merely vague notions of utility or satisfaction, there must exist a number of actual or virtual locations where the output of production can be sold. This is the most obvious function of markets in the real system, and hence the crucial functions of marketing and advertising in actual business. If the output cannot be sold there can be no profit. Having established this as the main point, it then could then be conceded that markets also do serve the regulatory/validating function (over)emphasized by neoclassical economics, and which, for that matter, also appears in the old Marxian notion of "socially necessary labor time". If someone, somewhere, is eventually prepared to *buy* the output of the producer, presumably the effort that went into its production was indeed "socially necessary", at least in the opinion of the purchaser at the time of sale.

The role of entrepreneurial business in the system, finally, is to organize productive activity in the pursuit of profits. The term business is used here in a generic sense, including all types of business organization, the individual entrepreneur, partnerships and all corporate forms. It might have been adequate to use the term "business operations" here, following Heinsohn and Steiger (2000). However, the qualifier "entrepreneurial" is employed to recognize the point, stressed by both Schumpeter and Keynes that, *given* an accommodative framework provided by the other institutions, particularly financial institutions, the essence of the system is *then* the incentive for innovation and dynamic change. There are, clearly, a number of difficulties in describing the different practical variations on the method of enterprise that arise because of the different forms of business organization. Identifying the profit or surplus in accounting terms in practice is much complicated by the different regulations in place in different jurisdictions, and by different systems of corporate governance. If, for example, the shareholders of a company are the same persons as those actually controlling the firm then any dividend payments that they receive may genuinely be counted as part of the profit. In contrast, if the shareholders are purely passive, then the actual managers of the firm may well view dividends as just another element of cost, really quite similar to interest payments, (albeit with a different contractual and "risk" status).[5] In this case, we would have to look for the genuine surplus or profit in such areas as retained earnings, the salaries, bonuses, and prerequisites of the top management, and possibly also consumption-type spending by the firm itself (Smithin 2009).

However, if we were alternatively discussing the generic type of the traditional economy or command economy, for example, there would also be a great many practical and/or historical variations that would have to be taken into account in any discussions of "cases". However, this would not detract in any way from the value of discussions of the "ideal type" itself (Heilbroner 1999, Ingham 2004, Smithin 2009). According to Smithin (2009):

> These are empirical rather than theoretical issues. For them to come up for discussion at all, for there to be any debate about how the surplus is distributed, there must be a profit surplus in existence in the first place.

One of the conditions of there being a profit surplus, moreover, is the *real* existence of the monetary/financial system itself.

Conclusion

It may seem that Geoffrey Ingham's work, taken as a whole, opens something of a Pandora's Box for scholars in the established disciplines, with all sorts of unwanted problems unleashed on the intellectual world and the creation of numerous additional onerous tasks for the conscientious scholar to perform.

However, the last thing released from Pandora's Box (actually Pandora's Jar, as classical scholarship insists) was Hope. In this case, I suppose, hope that it will eventually be possible to obtain a better understanding of the large subject of which Ingham himself (2005/1996) once said (quoting Ganssmann, quoting Marx, *misquoting* Gladstone):

> …even love has not turned more men into fools than meditation on the nature of money.

I have tried to show in this chapter that this need not be the case, particularly if we follow the leads set down by Geoffrey Ingham himself in subsequent work.

Notes

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2. According to Smithin (2011), "the latter cannot be understood in isolation from the former".

3. For the opposite view see (*e.g.*) Dobb (1973). See also several of the essays in Harcourt (2012).

4. King (2012) does explicitly endorse the work of Michal Kalecki (*e.g.,* 1971) as an exemplar of the sort of theory that might be useful in bridging the double gap.

5. The term "risk" is placed in quotes here because of the hopeless confusion that prevails everywhere over the use of this term in the financial and economic context. This arises from the inability to distinguish the theorems of statistical probability theory from the concept of fundamental uncertainty (Davidson 2009).

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